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In the Supreme Court of the United States

OCTOBER TERM, 1972

No. ____

FEDERAL POWER COMMISSION, PETITIONER

v.

MEMPHIS LIGHT, GAS AND WATER DIVISION, ET AL.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

The Solicitor General, on behalf of the Federal Power Commission, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

OPINIONS BELOW

The initial opinion of the court of appeals (App. A, *infra*, pp. 17–39) and its opinion on rehearing (App. B, *infra*, pp. 41–53) are not yet reported. The initial opinion (No. 578) of the Federal Power Commission (App. D, *infra*, pp. 57–66) and its opinion on rehearing (No. 578–A; App. E, *infra*, pp. 67–71) are reported at 43 FPC 824 and 44 FPC 140.

JURISDICTION

The judgment of the court of appeals was entered on February 18, 1972 (App. C, *infra*, pp. 55–56), and the Commission's petition for rehearing was denied on May 11, 1972 (App. B, *infra*, pp. 41–53). On August 4, 1972, the Chief Justice extended the time for filing a petition for a writ of certiorari to September 23, 1972. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

STATUTE INVOLVED

Section 441 of the Tax Reform Act of 1969, 83 Stat. 625, 26 U.S.C. 167(l), is set forth in App. F, *infra*, pp. 73–78.

QUESTION PRESENTED

Whether, in enacting Section 441(a) of the Tax Reform Act of 1969, Congress intended to withdraw from the Federal Power Commission and other agencies charged with similar regulatory responsibilities the authority to permit a utility, in calculating its federal income tax allowance for ratemaking purposes, to conform its method of computing depreciation on its other property to the method it had elected under the Act to be applicable to its post-1969 expansion property.[1]

[1] If this Court grants certiorari, we intend to argue further that, assuming Section 441(a) did not affect the Commission's authority to permit a utility to conform its depreciation methods, the Commission's action in this case was proper and should be affirmed without further proceedings in the court of appeals.

STATEMENT

It has long been established that federal income taxes are properly includable as an expense under the cost of service method of ratemaking utilized by the Federal Power Commission in the regulation of rates for sales of natural gas subject to its jurisdiction under the Natural Gas Act, 15 U.S.C. 717, *et seq.* The method of calculating such taxes for ratemaking purposes, however, may not be the same as the method used for calculating the taxes actually paid. In the instant rate proceeding, the Commission determined that nothing in Section 441(a) of the Tax Reform Act of 1969, 26 U.S.C. 167(*l*)—which Section specifies the depreciation methods utilities may use in calculating their federal income taxes—deprives it of the authority to permit a company subject to its jurisdiction to shift from liberalized depreciation with flow-through to liberalized depreciation with normalization[1] with respect to pre-1970 property and post-1969 replacement property (collectively referred to herein-

[1] Under flow-through, a utility using liberalized (accelerated) depreciation in calculating its actual taxes, also uses liberalized depreciation in calculating its tax expense for ratemaking purposes. Actual current tax savings are thus "flowed-through" to the utility's customers. Under normalization, taxes for ratemaking purposes are computed using straight-line depreciation although the utility uses liberalized depreciation in calculating the taxes it actually pays. The difference between the taxes that would have been paid under straight-line depreciation and the actual taxes based on liberalized depreciation is put into a deferred tax reserve account by the utility to pay future taxes.

Not involved in this proceeding is the accounting method used by the utility for calculating depreciation as a separate, non-tax expense to be reflected in establishing rates.

after as "existing property"). Focusing on a provision in Section 441(a) of the Act which by its terms applies only to post-1969 expansion property (26 U.S.C. 167(*l*)(4)(A)), the court of appeals reversed the Commission.

A. BACKGROUND

With the adoption of Section 167 of the Internal Revenue Code of 1954, 68A Stat. 51, companies for the first time were authorized to use liberalized or accelerated depreciation in calculating their federal income taxes. The Commission at first determined that the use of liberalized depreciation merely resulted in a tax deferral and, to avoid benefiting the present customers of a utility at the expense of later customers who would have to pay the deferred taxes, the Commission decided that the income tax expense allowed as a cost of service for ratemaking purposes should be normalized—*i.e.*, computed as if the company were using straight-line depreciation. See *Amere Gas Utilities Co.*, 15 FPC 760, 781; *Cities of Lexington, etc., Ky. v. Federal Power Commission*, 295 F.2d 109, 114 (C.A. 4).

In *Alabama-Tennessee Natural Gas Co.*, 31 FPC

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[1] Section 441(a) of the Tax Reform Act added subsection (*l*) to Section 167 of the Internal Revenue Code, 26 U.S.C. 167(*l*). Section 167(*l*)(3)(B) and (C) distinguishes between pre-1970 property, or property acquired before January 1, 1970, and post-1969 property, or property acquired on January 1, 1970, or after. Section 167(*l*)(4)(A) establishes an additional category of post-1969 property which "increases the productive or operational capacity of the taxpayer * * * and does not represent the replacement of existing capacity," referred to hereinafter as "expansion property."

308, affirmed *sub nom. Alabama-Tennessee Natural Gas Co. v. Federal Power Commission*, 359 F.2d 318 (C.A. 5), certiorari denied, 385 U.S. 847, the Commission reconsidered the issue and found that the use of liberalized depreciation by utilities usually resulted in permanent tax savings since most utilities had growing or stable plant investments.[4] Accordingly, the Commission ordered utilities using liberalized depreciation to flow-through to their customers the resultant tax savings.[5] Finally, in *Midwestern Gas Transmission Co.*, 36 FPC 61, affirmed *sub nom. Midwestern Gas Transmission Co. v. Federal Power Commission*, 388 F.2d 444 (C.A. 7), certiorari denied, 392 U.S. 928, the Commission held that for rate-making purposes it would impute the use of liberalized tax depreciation to any company which shifted from liberalized tax depreciation to straight-line depreciation and would flow through the resulting imputed tax savings to the company's customers.

B. SECTION 441(a) OF THE TAX REFORM ACT OF 1969

In considering tax reform legislation in 1969, the House Ways and Means Committee expressed concern over the loss of tax revenues resulting from shifting by regulated utilities either from straight-

[4] A growing company using liberalized depreciation generally has enough new and replacement property to generate sufficient depreciation allowances to offset the declining depreciation allowances on its existing property.

[5] In the same case, the Commission initiated the policy now in effect that the deferred tax reserve accumulated by a utility that had been using normalization must be deducted from the utility's rate base so that no return on the tax savings would be included in its rates. 31 FPC at 220–221.

line depreciation to liberalized depreciation or from liberalized depreciation with normalization to liberalized depreciation with flow-through; the committee also cited with disapproval the practice of several regulatory agencies of imputing for ratemaking purposes the use of liberalized depreciation with flow-through to utilities using straight-line depreciation for tax purposes. H. Rep. No. 91-413, 91st Cong., 1st Sess., pp. 131-132. On the other hand, the House committee rejected suggestions by the Commission and others that all utilities using liberalized depreciation be required to change to straight-line depreciation, since such a rule would place some utilities at a competitive disadvantage and would result in substantial rate increases (*id.* at 132). Accordingly, the committee proposed and the House passed a "freeze" on existing depreciation practices subject to the following three general rules (*id.* at 133):

> (1) If straight line depreciation is presently being taken, then no faster depreciation is to be permitted as to that property.
>
> (2) If the taxpayer is taking accelerated depreciation and is "normalizing" its deferred taxes, then it must go to the straight line method unless it continues to normalize as to that property.
>
> (3) If the taxpayer is taking accelerated depreciation and flowing through to its customers the benefits of the deferred taxes, then the taxpayer must continue to do so, unless the appropriate regulatory agency permits a change as to that property.

The Senate Committee on Finance, while also expressing concern over the loss of tax revenues from utility depreciation practices, similarly rejected a requirement that all utilities revert to straight-line depreciation. S. Rep. No. 91–552, 91st Cong., 1st Sess., pp. 172–173. The committee proposed and the Senate passed legislation similar to the House bill, except that utilities on flow-through were given the right to elect within 180 days of the enactment of the bill

> * * * to shift from the flow-through to the straight-line method, with or without the permission of the appropriate regulatory agency, or * * * with the permission of the regulatory agency to shift to the normalization method (that is, to come under general rules of the bill). [*Id.* at 173.]

In conference, the Senate bill was amended to limit the right of election to expansion property. See H. Conf. Rep. No. 91–782, 91st Cong., 1st Sess., pp. 312–313. As thus amended, the depreciation provisions were enacted as Section 441(a) of the Tax Reform Act of 1969.

C. PROCEEDINGS BEFORE THE COMMISSION

Following enactment of the Tax Reform Act of 1969, the Texas Gas Transmission Corporation, in the context of pending rate proceedings, advised the Commission of its intent to elect under Section 441(a) of the Act to abandon flow-through with respect to its expansion property and, with the Commission's permission, to use liberalized depreciation with normalization with respect to such property in computing its

federal income tax (App. D, *infra*, p. 59). Before it made the election, however, Texas Gas sought permission to change from flow-through to straight-line depreciation or, preferably, liberalized depreciation with normalization with respect to its existing property (*ibid.*).

In Order No. 404, 43 FPC 740, rehearing denied, 44 FPC 16, the Commission announced that as a general policy it would permit utilities making the election under Section 441(a) of the Tax Reform Act to use liberalized depreciation with normalization with respect to their expansion property.

Subsequently, the Commission issued Opinion No. 578 in Texas Gas' pending rate proceedings permitting Texas Gas to shift to liberalized depreciation with normalization with respect to all its property (App. D, *infra*, pp. 57–66). The Commission found that once Texas Gas had elected to abandon flow-through with respect to its expansion property, the continued use of flow-through with respect to its existing property would result in a steadily increasing tax expense for ratemaking purposes, since liberalized depreciation on new facilities would no longer be available to offset declining depreciation on existing facilities (App. D, *infra*, pp. 62–63). The Commission concluded that the use of normalization with respect to Texas Gas' existing property was necessary to promote stable rates (App. D, *infra*, p. 63).

In accordance with its established practice (see n. 5, *supra*), the Commission required Texas Gas to put the difference between the taxes actually paid and the taxes that would have been paid under

straight-line depreciation (and are claimed as a cost of service for ratemaking purposes) into a deferred tax reserve. The reserve was required to be deducted from the rate base so that the company would not earn any return on the reserve (App. D, *infra*, p. 65).[6]

D. THE DECISION BELOW

Petitions for review were filed with respect to both Order No. 404 and Opinion 578 and were consolidated by the court of appeals. The court upheld the Commission's decision in Order No. 404 to permit utilities electing to abandon flow-through with respect to their expansion property to use liberalized depreciation with normalization on such property (App. A, *infra*, pp. 20–29).[7]

The court below reversed the Commission, however, with respect to Opinion No. 578; it held that Section 441(a) of the Tax Reform Act deprived the Commission of authority to permit utilities to abandon flow-through with respect to their existing property (App. A, *infra*, pp. 29–39). The court recognized that the original version of the legislation adopted by the House did not limit this authority, but construed the election provision proposed by the Senate and nar-

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[6] Texas Gas' customers would thus benefit indirectly from the use of liberalized depreciation with normalization, since the reserve provides the company with capital for the expansion of facilities or the improvement of service at no cost to the customers.

[7] A petition for a writ of certiorari to review this aspect of the decision below is pending. *Memphis Light, Gas and Water Division* v. *Federal Power Commission, et al.*, No. 72-96. We have filed a brief in opposition to the petition.

rowed in conference as a limitation on the House bill (App. A, *infra*, pp. 31–34). In denying petitions for rehearing, the court reaffirmed its interpretation of Section 441(a) and its legislative history (App. B, *infra*, pp. 41–53).

REASONS FOR GRANTING THE WRIT

The decision below erroneously construes Section 441(a) of the Tax Reform Act of 1969 to prohibit the Federal Power Commission from permitting a utility, in calculating its federal income tax allowable as a cost of service for ratemaking purposes, to conform its method of computing depreciation on existing property to its method of computing depreciation on expansion property. The decision seriously impairs the ability of the Commission and other regulatory agencies[*] to prescribe rational accounting practices and promote stable rates. Accordingly, review by this Court is warranted.

1. Prior to the enactment of the Tax Reform Act of 1969, the Commission exercised broad authority over the methods that electric utilities and natural gas companies subject to its jurisdiction employed to compute depreciation in calculating federal income taxes as a cost of service for ratemaking purposes (see pp. 4–5, *supra*). While Section 441(a) of the 1969 Act

[*] Section 441(a) applies to all property used predominantly to furnish or sell (1) electric energy, water or sewage disposal services, (2) gas or steam through a local distribution system, (3) telephone and certain other communication services, and (4) transportation of gas or steam by pipeline, if the rates for such services are regulated. 26 U.S.C. 167(*l*)(3)(A).

restricts that authority in certain respects,' neither the statute nor its legislative history supports the restriction on the Commission's authority over accounting practices with respect to existing properties imposed by the court of appeals.

As we have noted (see p. 6, *supra*), the initial House version of Section 441(a) embodied three general rules with respect to depreciation practices, the third of which required a utility using liberalized depreciation with flow-through on its existing property to continue using that method of depreciation, "unless the appropriate regulatory agency permits a change as to that property." H. Rep. No. 91-413, *supra*, p. 133. The Senate report makes clear that the Senate amendments followed the House bill with respect to existing property, except that the Senate also gave utilities the right to elect to abandon flow-through. The Senate report states (S. Rep. No. 91-552, *supra*, pp. 172-173):

> Both the House bill and the committee amendments provide that in the case of existing property the following rules are to apply:
>
> * * * * *
>
> (3) If the taxpayer is taking accelerated depreciation and flowing through to its customers the benefits of the deferred taxes, then the taxpayer would continue to do so (except as provided under the committee amendments which

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*The election provision in Section 441(a), 26 U.S.C. 167(*l*)(4)(A), for example, prohibits the Commission from imputing the use of liberalized depreciation with flow-through for expansion property to utilities electing to abandon flow-through with respect to such property. See our brief in opposition in No. 72-96 (n. 7, *supra*).

are discussed below), unless the appropriate regulatory agency permits a change as to that property.

The parenthetical reference is to the right of election. In other words, the right of election adopted by the Senate simply provides an additional procedure whereby utilities may get off flow-through with respect to existing property, but does not restrict the authority of regulatory agencies generally to permit the abandonment of flow-through. Thus, when the conference restricted the right of election to expansion property, but otherwise followed the Senate amendments (H. Conf. Rep. No. 91-782, *supra*, pp. 312-313), it did not disturb the regulatory authority recognized by the general rules referred to in the House and Senate reports. See General Explanation of the Tax Reform Act of 1969, H.R. 13270, 91st Congress, Public Law 91-172, prepared by the staff of the Joint Committee on Internal Revenue Taxation, p. 153."

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[10] As finally enacted, Section 441(a) adds a new subsection (*l*) to Section 167 of the Internal Revenue Code of 1954, 26 U.S.C. 167(*l*), prescribing what constitutes a "reasonable allowance" for depreciation of public utility property for computing the depreciation deduction under Section 167(a). Under Section 167(*l*)(1), a "reasonable allowance" for pre-1970 property is an allowance computed under either (1) a "subsection (*l*)" (essentially straight-line, see Section 167(*l*)(3)(F)) method, (2) the method used prior to the enactment of the bill if the company uses normalization, or (3) accelerated depreciation with flow-through if the company used flow-through on such property prior to the enactment of the bill. Under Section 167(*l*)(2), a "reasonable allowance" for post-1969 property is an allowance computed in one of three ways: (1) under a "subsection (*l*)" method, (2) under accelerated depreciation with normalization or (3) under accelerated

In reaching the contrary conclusion, the court below placed greater emphasis (App. A, *infra*, p. 33) on the following sentence in the second paragraph of the Conference report's discussion of the depreciation provisions (H. Conf. Rep. No. 91–782, *supra*, p. 312):

> This rule [that a taxpayer cannot use accelerated depreciation unless it normalizes] is not to apply in the case of a taxpayer that is at present flowing through the tax reduction to earnings for purposes of computing its allowable expenses on its regulated books of account.

The court construed "This rule" to refer to the final version of the statute as approved by the conference and thus concluded that there was no way a utility could get off flow-through with respect to existing property. A close reading of the report, however, discloses that "This rule" does not refer to the final bill, but refers to the initial House bill summarized in the first two paragraphs of the report's discussion of the depreciation provisions; the third paragraph discusses the Senate amendments and only the fourth paragraph explains the conference modifications of the legislation. When the first two paragraphs are read together, the above-quoted sentence is seen to state merely that a company on flow-through *may* remain on flow-through; it does *not* state—what even the court below conceded the House bill did not provide—that a company on flow-through could not

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depreciation with flow-through if the utility used flow-through on similar property prior to the enactment of the bill. Under the election provision, Section 167(*l*)(4)(A), a utility may elect not to have the third option (accelerated depreciation with flow-through) apply to its post-1969 expansion property.

abandon flow-through with respect to its existing property with the permission of the appropriate regulatory agency.

The court below also emphasized the statements in the House and Senate reports that the proposed legislation was intended to "freeze" the current situation regarding methods of depreciation (App. A, *infra*, pp. 34-35). This emphasis is misplaced and does not support the decision below. As shown above, both reports specifically indicate that a utility may abandon accelerated depreciation with flow-through on existing property with the permission of the appropriate regulatory agency. Thus, while Congress imposed a "freeze" so that utilities would not be required to abandon flow-through and force automatic rate increases, it did not deny regulatory agencies the authority to determine whether in particular instances the abandonment of flow-through accounting is in the public interest.

2. In this case, the Commission properly concluded that it was not in the public interest for Texas Gas to compute its federal tax expense for ratemaking purposes using normalization on expansion property and flow-through on existing property. If the different methods of depreciation were used, liberalized depreciation on expansion facilities would no longer be available to offset declining depreciation on existing facilities.[11] As a result, the depreciation deduction

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[11] As we have noted, "existing property" includes replacement property (see n. 3, *supra*). Liberalized depreciation on replacements would not offset declining depreciation on the property remaining in service, however, since the nature of

would steadily decrease and the tax expense for rate-making purposes would increase necessitating periodic rate increases. In these circumstances, it was well within the competence and authority of the Federal Power Commission to determine that the use of the same method of depreciation for both expansion and existing property, while perhaps necessitating present rate increases (rather than deferral to future consumers of payments for present tax expenses), would promote stable rates and would be in the public interest.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

ERWIN N. GRISWOLD,
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SEPTEMBER 1972.

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the pipelines and other equipment used by the natural gas industry is such that replacements are relatively infrequent and may not be necessary until well after an asset is fully depreciated (see App. D, *infra*, pp. 62–63).

APPENDIX A

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S.App.D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 24,517

MEMPHIS LIGHT, GAS AND WATER DIVISION, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION,
TENNESSEE VALLEY MUNICIPAL GAS ASSOC., ETC., INTERVENORS

No. 24,518

MEMPHIS LIGHT, GAS AND WATER DIVISION, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION,
AMERICAN PUBLIC GAS ASSOCIATION, INTERVENORS

No. 24,602

TENNESSEE VALLEY MUNICIPAL GAS ASSOCIATION, ET AL., PETITIONERS

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION, INTERVENOR

No. 24,632

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION, INTERVENOR

Petitions for Review of Orders of the Federal Power Commission

Decided February 18, 1972

Mr. George E. Morrow, with whom *Mr. Reuben Goldberg* was on the briefs, for petitioner in Nos. 24,517 and 24,518.

Mr. Morton L. Simons for petitioner in No. 24,632.

Mr. J. Richard Tiano, Assistant Solicitor, Federal Power Commission, with whom *Messrs. Gordon Gooch*, General

Counsel, and *Abraham R. Spalter*, Assistant General Counsel, Federal Power Commission, were on the brief, for respondent. *Mr. Israel Convisser*, Attorney, Federal Power Commission, also entered an appearance for respondent.

Mr. Christopher T. Boland, with whom *Mr. Richard J. Connor* was on the brief, for intervenor Texas Gas Transmission Corporation. *Mr. George J. Meiburger* also entered an appearance for intervenor Texas Gas Transmission Corporation in Nos. 24,517 & 24,518.

Mr. Reuben Goldberg entered an appearance for petitioner in No. 24,602.

Mr. Charles F. Wheatley, Jr., was on the brief for intervenor American Public Gas Association in No. 24,518.

Before FAHY, *Senior Circuit Judge*, and ROBINSON and WILKEY, *Circuit Judges*.

WILKEY, *Circuit Judge*: These two sets of cases, consolidated for review, involve a determination as to the impact of Section 441(a) of the Tax Reform Act of 1969,[1] relating to the methods of depreciation for regulated utilities, on two types of utility property: (1) post-1969 expansion property and (2) pre-1970 and post-1969 non-expansion property.[2] The impact of Section 441(a) on post-1969 ex-

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[1] Int. Rev. Code of 1954, § 167(l), *as amended* Publ. L. 90-26, §§ 1, 2(b), 81 Stat. 57, 58 (1967); Publ. L. 91-172, § 521 (a), (d), 83 Stat. 625, 649, 653 (1969).

[2] Section 441(a) of the 1969 Tax Reform Act defines "pre-1970" property as "property which was public utility property in the hands of any person at any time before January 1, 1970." [Int. Rev. Code of 1954, § 167(l)(3)(B)]. Property which is not pre-1970 is considered "post-1969" property [Int. Rev. Code of 1954, § 167 (l)(3)(C)]. "Expansion" property is the term employed to denote that property "which increases the productive or operational capacity of the taxpayer," while "non-expansion" property refers simply to

pansion property—the subject of FPC Orders No. 404 and 404-A, issued, respectively, 15 May 1970 and 9 July 1970, and cases no. 24,518 and 24,602 here—will be considered first, followed by a determination of its effect on pre-1970 and post-1969 non-expansion property—the subject of FPC Opinions No. 578 and 578-A and accompanying orders, issued 3 June 1970 and 21 July 1970, respectively, and cases no. 24,517 and 24,632 here.

I.

A.

Congress specifically provided for the proper depreciation treatment of post-1969 utility expansion property in Section 441(a) of the Tax Reform Act of 1969 as follows:

> (A) *Election as to new property representing growth in capacity.*—If the taxpayer makes an election under this subparagraph within 180 days after the enactment of this subparagraph in the manner prescribed by the Secretary or his delegate, in the case of taxable years beginning after December 31, 1970, paragraph (2)(C) [concerning liberalized depreciation with flow-through] shall not apply with respect to any post-1969 public utility property, to the extent that such property constitutes property which increases the productive or operational capacity of the taxpayer with respect to the goods or services described in paragraph (3)(A) and does not represent the replacement of existing capacity.[1]

This provision indicates that Congress intended to, and did, prescribe specifically the appropriate tax depreciation treatment for post-1969 expansion property of utilities such as involved in the cases here. It permits a regulated utility such as Texas Gas Transmission Corporation,

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that property which replaces the existing plant of a taxpayer [Int. Rev. Code of 1954 § 167(1)(4)(A)].

[1] Int. Rev. Code of 1954, § 167(1)(4)(A).

an intervenor in these cases, to make an election, within 180 days after enactment of this provision, *not* to have liberalized depreciation with flow-through[4] apply with respect to its post-1969 expansion property. That is, such a method would no longer be considered a "reasonable allowance" for tax depreciation purposes within the meaning of the Internal Revenue Code of 1954.[5]

The legislative history accompanying Section 441(a) of the 1969 Tax Reform Act supports this interpretation. The report of the Senate Finance Committee states in relevant part:

> The [Senate] committee amendments, while in most respects the same as the House provisions, differ in one principal area. The amendments permit an election to be made within 180 days after the date of enactment of the bill for a utility covered by this provision to shift from the flow-through to the straight-line method, *with or without the permission of the appropriate regulatory agency, or permit it with the permission of the regulatory agency to shift to the normalization method* (that is, come under general rules of the bill).
>
> *This election applies both as to new and existing property.* . . . Since the company would no longer be permitted to use accelerated depreciation (unless the agency later permits it to normalize), the agency

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[4] By utilizing liberalized depreciation in computing its income tax, a utility obtains a larger deduction, and thus pays less income tax, at least initially, and, in the case of expanding or steady plants, overall, than it would if it used straight-line depreciation. Under the "flow-through" method of liberalized depreciation, a utility is allowed to recoup from its customers by means of its rates only the taxes it *actually* pays; under "normalization," however, it is allowed to recoup the higher taxes it would pay (but actually does not) if it were using straight-line depreciation.

[5] Int. Rev. Code of 1954, § 167(1)(2)(C).

would not be able to impute the use of accelerated depreciation with flow-through.[6]

In conference, the *election right was restricted to apply only to post-1969 expansion property.* As the Conference Report indicates:

> The conference substitute (sec. 441 of the substitute and sec. 167(1) of the code) *follows the Senate amendment except that* the special provision referred to in (e) above is stricken and *the 180-day election (item (d), above) is modified to apply to new property and not to replacement property.* Even in the case of new property, however, the right to change over from the flowthrough method is to be available only to the extent the new property increases the productive or operational capacity of the company.[7]

It is clear, then, that Congress intended to, and did in fact, provide regulated utilities such as Texas Gas with an option to abandon flow-through for rate-making purposes in regard to post-1969 expansion property and substitute in its place either (1) straight-line depreciation, with or without the permission of the relevant regulatory agency or (2) accelerated depreciation with normalization,[8] with

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[6] S. Rep. No. 552, 91st Cong., 1st Sess. 173-74 (1969) (emphasis added).

[7] Conf. Rep. No. 782, 91st Cong., 1st Sess. 312-13 (1969) (emphasis added).

[8] Under normalization, taxes for *rate-making purposes* are determined on the basis of straight-line depreciation, while for *tax purposes* liberalized depreciation is used. The differences between the taxes which would be payable under straight-line depreciation and the taxes payable under liberalized depreciation is placed into a deferred tax reserve account by the taxpayer. The FPC requires that this reserve account be deducted from the rate base. Accordingly, the rates charged customers are lower by the amount of the return on this reserve account which would otherwise be charged if the reserve account were not deducted from the rate base.

the permission of the appropriate regulatory agency. It is also clear that Congress intended thereby to preclude regulatory agencies from imputing flow-through to any regulated utility exercising this election with respect to its post-1969 expansion property.[9]

B.

The basic issue in this set of cases, therefore, is whether the FPC was correct in its Orders No. 404 and 404-A in interpreting the Tax Reform Act of 1969 as depriving it of the power to impute the use of liberalized depreciation with flow-through for rate-making purposes to a utility making the election under Section 441(a)[10] to abandon flow-through with respect to its post-1969 expansion property. Clearly, it is the duty of the FPC, under its Congressional mandate, the Natural Gas Act,[11] to ensure the

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[9] As the Senate Finance Committee Report states with respect to a company exercising its right to abandon flow-through under the 180-day election provision, ". . . Since the company would no longer be permitted to use accelerated depreciation (unless the agency later permits it to normalize), *the agency would not be able to impute the use of accelerated depreciation with flow-through.*" [See note 6, *supra*, at 174 (emphasis added)] While the availability of the 180-day election option was subsequently limited in conference to apply only to post-1969 utility expansion property, the Conference Report stated that "[t]he conference substitute (Sec. 441 of the substitute and Sec. 167(1) of the code) *follows the Senate amendment* except that "the 180-day election . . . is modified to apply to new property and not to replacement property." [See note 7, *supra* (emphasis added)] This indicates that the Senate rationale, cited above, is controlling as to post-1969 expansion property, thus preventing the Commission from imputing liberalized depreciation with flow-through to Texas Gas' post-1969 expansion property.

[10] See note 8, *supra*.

[11] 15 U.S.C. §§ 717-717(w) (1954).

continued availability of natural gas in interstate commerce for eventual sale to consumers at the lowest practicable rate. As the Fifth Circuit had occasion to observe:

> The central principle in the regulation of the natural gas industry around which all ratemaking revolves is "the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption . . . at the lowest possible reasonable rate consistent with the maintenance of adequate service on the public interest."

This is the language of Section 7(c) of the Natural Gas Act as originally enacted in 1938. The provision was deleted when the subsection was amended in 1942 but, as the Supreme Court has held, the amendment was not intended to change the congressional purpose of the Act; the "primary aim of this legislation was to protect consumers against exploitation at the hands of natural gas companies." *Federal Power Commission* v. *Hope Natural Gas Company*, 1944, . . . Again, as Justice Clark reiterated twenty-five years later: "The Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges." *Atlantic Refining Company* v. *Public Service Commission*, 1959, . . .[12]

However, the FPC may not remain oblivious to the wishes of Congress as expressed in forms other than amendments to or deletions from the Natural Gas Act. By means of Section 441(a) of the 1969 Tax Reform Act, Congress has provided regulated utilities such as Texas Gas with an absolute right of election to abandon flow-through with respect to their post-1969 expansion property. Furthermore, we do not have the situation presented in *Alabama-Tennessee Natural Gas Co.* v. *FPC*,

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[12] *Alabama-Tennessee Natural Gas Co.* v. *Federal Power Commission*, 359 F.2d 318, 331 (5th Cir.), *cert. denied* 385 U.S. 847 (1966).

supra, where the court was able to find "no evidence that at the time Section 167 [of the Internal Revenue Code] was enacted Congress even focused on the problem in terms of reducing the dimensions of the Federal Power Commission's regulatory responsibility to protect consumers from excessive rates. . . ."[12] Rather, investigation of the legislative history regarding Section 441(a) of the Tax Reform Act of 1969 reveals that Congress was well aware of the implications of permitting regulated utilities an election to abandon liberalized depreciation with flow-through with respect to the their post-1969 expansion property.[14] As such, the FPC was not remiss in the performance of its statutory duty in permitting Texas Gas to abandon flow-through in regard to its post-1969 expansion property, as expressly provided by the language of Section 441(a) of the 1969 Tax Reform Act.

C.

The FPC's Orders No. 404 and 404-A, indicating that it would continue the policy adopted in *Alabama-Tennessee Natural Gas Co., supra*,[15] of deducting the amounts in the accrued deferred tax account from the rate base and not considering such balances as part of capitalization in rate proceedings before it, is a statement of policy based essentially on an interpretation of Section 441(a) of the 1969 Tax Reform Act. Thus, under the pertinent provi-

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[12] *Id.*, at 332. As the court also observed, "Occam's razor slices through the arguments based on legislative history and congressional intent. Either Congress did not consider the concrete problem the case presents or, if it did, Congress decided to let sleeping dogs lie." [*Id.*, at 336]

[13] See notes 6 & 7, *supra*.

[14] 31 FPC 208, *modified* 31 FPC 923 (1964), *aff'd sub nom. Alabama-Tennessee Natural Gas Co.* v. *Federal Power Commission*, see note 12, *supra*.

sions of the Administrative Procedure Act,[16] it was properly issued without notice or opportunity for hearing, since it was not the result of a rulemaking proceeding.

While Memphis Light contends that Orders No. 404 and 404-A of the Commission denied them the benefits of liberalized depreciation with flow-through accounting and ratemaking in regard to their post-1969 expansion property, they misdirect their attack. Instead of the Commission's orders here, what resulted in the denial of liberalized depreciation with flow-through was the election by Texas Gas to abandon such depreciation, as it was specifically entitled to do under Section 441(a) of the 1969 Tax Reform Act. Texas Gas made this election in a letter to the Commissioner of Internal Revenue dated 8 June 1970, a copy of which was transmitted to the FPC dated 10 June 1970. At this juncture, the *only* options available to the Commission were either to do nothing and thereby leave Texas Gas on straight-line depreciation or to permit it to use liberalized depreciation with normalization. And the FPC chose the latter.

The Commission's Orders No. 404 and 404-A, then, were nothing more than statements of FPC policy interpreting the mandate of Congress as expressed in Section 441(a) of the Tax Reform Act of 1969. As such, they were clearly exempt from the notice and opportunity for hearing requirements for rulemaking provided under the Administrative Procedure Act. While it is true that the FPC's interpretative rulings here may have significant economic consequences on Memphis Light and other ratepayers in the long run, such a statement of policy is specifically exempted by the Administrative Procedure Act from the need for prior notice or opportunity for a hearing:

> Except when notice or hearing is required by statute [not relevant here], this subsection does not apply—

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[16] 5 U.S.C. § 553(b)(A) (1966).

(A) to interpretative rules, *general statements of policy*, or rules of agency organization, procedure, or practice. . . ."[17]

D.

The case law does not support the petitioners' assertion that notice and opportunity for hearing were required in this set of cases—24,518 and 24,602. While interested parties might argue the validity of the FPC's interpretation of Congressional purpose as expressed in Section 441(a) of the Tax Reform Act of 1969, such an opportunity is not required by the Administrative Procedure Act prior to issuance of such interpretations by an administrative agency.[18]

The petitioners' argument that the FPC, as a result of the issuance of its Orders No. 404 and 404-A, has changed its policy in *Alabama-Tennessee Natural Gas Co., supra*, is incorrect. Only those utilities that made the election provided by Section 441(a) of the 1969 Tax Reform Act to abandon flow-through with respect to their post-1969 expansion property are affected by the Commission orders here at issue. The case of *Texaco, Inc.* v. *FPC*[19] is inapposite, since the switch from simple to compound interest which the Commission ordered in that case was one involving consideration of, *inter alia*, current interest rates and trends, the impact on individual companies and the effect of increased contingent liabilities on the ability of the companies affected to acquire new equity or debt capital. In contrast, the instant set of cases, aside from the question of the validity of the FPC's interpretation of

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[17] *Id.* (emphasis added).

[18] *See Id.*; also, *Gibson Wine Co.* v. *Snyder*, 90 U.S. App. D.C. 135, 194 F.2d 329 (1952); *Garelick Manufacture Co.* v. *Dillon*, 114 U.S. App. D.C. 218, 313 F.2d 899 (1963).

[19] 412 F.2d 740 (3rd Cir. 1969).

Section 441(a) of the 1969 Tax Reform Act, involved no need for further consideration by the Commission as to what regulatory policy would result in a lower rate for Memphis Light and other ratepayers. The impact of liberalized depreciation with normalization as opposed to that of straight-line depreciation—the only choice open to the FPC under the election provision for regulated utilities such as Texas Gas contained in Section 441(a) of the 1969 Tax Reform Act, had already been fully considered and resolved in prior cases in favor of liberalized depreciation with normalization.[20]

The other principal case relied upon by the petitioners here, *National Motor Freight Traffic Association* v. *United States*,[21] is likewise inapposite. In that case, the Interstate Commerce Commission, after Congress had vested reparations authority in the courts in cases involving motor carriers, had announced an informal process for restoring to

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[20] See *Northern Natural Gas Co.*, 25 FPC 431 (1961), in which the Commission found that the use of liberalized depreciation with normalization provided tax benefits not available under straight-line depreciation. These benefits were shared with the ratepayers if a less-than-normal or zero rate of return was allowed on the tax reserve or if it was completely deducted from the company's rate base (as here) [25 FPC at 439-441]. In addition, the Commission in the instant set of cases, in denying petitions for rehearing, stated:

> The use of straight-line depreciation eliminates the possibility of tax deferrals to natural gas pipeline companies. On the other hand, liberalized depreciation with normalization may generate substantial tax deferrals. *The benefits of these tax deferrals are shared*, although admittedly not necessarily in equal proportions, *by the company and its customers* by treating such amounts as rate base deductions. [44 FPC 16 (1970) (emphasis added)]

[21] 268 F. Supp. 90 (D.D.C., three judges, 1967), *aff'd* 393 U.S. 18 (1968).

shippers past charges which were currently agreed by the carrier to have been illegal. This procedure did not relate to any substantive power specifically granted the ICC and the court in that case held that a rulemaking process was required to ascertain whether such authority existed in the first place and, if so, whether it should be exercised. In such a situation, unlike that presented by the set of cases at hand, the creation of procedures was an integral part of a substantive determination that could not be made without notice and opportunity for hearing. Here, however, since the only option open to the FPC was a choice between leaving a utility electing to abandon flow-through with respect to its post-1969 expansion property under Section 441(a) of the 1969 Tax Reform Act on straight-line depreciation, and, permitting it to use liberalized depreciation with normalization, hence, there was no need for prior notice or a hearing. Prior decisions of the Commission had already resolved this issue in favor of liberalized depreciation with normalization.[22]

II.

The second set of cases—24,517 and 24,632—involves the validity of the FPC's decision in its Opinions No. 578 and 578-A and accompanying orders, permitting Texas Gas to change from liberalized depreciation with flow-through to such depreciation with normalization in regard to its pre-1970 and post-1969 *non*-expansion property.

Section 441(a) of the Tax Reform Act of 1969 amended the Internal Revenue Code of 1954 by adding subsection (1), "Reasonable allowance in case of property of certain utilities," to Section 167 of the IRC. Section 441(a) distinguishes between two types of utility property: (1) pre-1970 and post-1969 non-expansion property and (2) post-1969 expansion property. With respect to the latter type,

[22] See note 20, *supra*.

Section 441(a) permits utilities using liberalized depreciation with flow-through to elect within 180 days of the enactment of Section 441(a) to shift either to straight-line depreciation of their own volition or to liberalized depreciation with normalization with the permission of the appropriate regulatory agency. Texas Gas exercised this option with respect to its post-1969 expansion property and received the FPC's permission to employ liberalized depreciation with normalization—the validity of which is treated in I., above.

In the instant set of cases, the determination of whether the FPC was correct in permitting Texas Gas to shift from liberalized depreciation with flow-through to similar depreciation with normalization with respect to its pre-1970 and post-1969 non-expansion property requires, first, a review of Section 441(a) and its legislative history to ascertain the intent of Congress here and, second, a consideration of the validity of the Commission's decision in light of this Congressional intent.

A.

Section 167(a) of the Internal Revenue Code of 1954[28] provides that a taxpayer is entitled to a "reasonable allowance" for a tax depreciation deduction. Section 441(a) of the 1969 Tax Reform Act specifies the appropriate methods for computing this "reasonable allowance" for pre-1970 and post-1969 non-expansion property in the case of regulated utilities such as Texas Gas. Under Section 441(a), a "reasonable allowance" may be computed in either of two ways: one, a "subsection (1) method," refers to the straight-line method of depreciation, while the other is "the applicable 1968 method for such property," but "only if the taxpayer uses a normalization method of

[28] Int. Rev. Code of 1954, § 167(a), ch. 736, 68A Stat. 51, as amended Publ. L. 89-800, § 2, 80 Stat. 1513 (1966).

accounting."[34] Section 441(a), however, provides an exception to the normalization requirement for using the second method by allowing a utility using the flow-through method to continue doing so.[35]

The right conferred on regulated utilities such as Texas Gas by Section 441(a) of the 1969 Tax Reform Act to make an election within 180 days of the enactment of Section 441(a) to shift from liberalized depreciation with flow-through to either straight-line depreciation or, with the approval of the appropriate regulatory agency, liberalized depreciation with normalization with respect to their post-1969 expansion property, as discussed in I., *supra*, does not, however, apply to pre-1970 and post-1969 non-expansion property.

The legislative history accompanying the enactment of Section 441(a) clearly reveals the intent of Congress that the right of election provided utilities to shift from liberalized depreciation with flow-through either to straight-line or to liberalized depreciation with normalization be confined simply to post-1969 expansion property. While the progress of Section 441(a) through both houses of Congress and in conference reveals the existence of differences as to what types of property should be made eligible under the election provision, *the final version of the bill limits the applicability of the right of election to post-1969 expansion (non-replacement) property alone.*

At the first stage, the House Report indicated:

> Your committee's bill provides that, in the case of *existing* property, the following rules are to apply:
>
> (1) If straight line depreciation is presently being taken, then no faster depreciation is to be permitted as to that property.

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[34] See note 1, *supra*, at § 167(1)(A).

[35] *Id.*, at § 167(1)(B).

(2) If the taxpayer is taking accelerated depreciation and is "normalizing" its deferred taxes, then it must go to the straight line method unless it continues to normalize as to that property.

(3) If the taxpayer is taking accelerated depreciation and is flowing through to its customers the benefits of the deferred taxes, then the taxpayer must continue to do so, unless the appropriate regulatory agency permits a change as to that property.[28]

Thus, under the House version of the bill, Texas Gas, since it had been using accelerated depreciation with flow-through, would have been required to continue doing so with respect to its "existing" (including replacement) property unless the Commission permitted otherwise. If this had been the law enacted, the Commission's and Texas Gas' position here would have been clearly justified. But, as we shall see, the law actually passed was significantly changed.

The bill as reported by the Senate Finance Committee gave regulated utilities using liberalized depreciation with flow-through an election to abandon that method of depreciation both for "pre-1970" property (a change from "existing" property in the House version) and "post-1969" property ("other" property in the House bill). The Senate Report states in regard to the altered right of election:

> The [Senate] committee amendments, while in most respects the same as the House provisions, differ in one principal area. The amendments permit an election to be made within 180 days after the date of enactment of the bill for a utility covered by this provision to shift from the flow-through to the straight-line method, with or without the permission of the regulatory agency, or permit it with the permission

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[28] H.R. Rep. No. 413 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 132-33 (1969) (emphasis added).

of the regulatory agency to shift to the normalization method (that is, to come under general rules of the bill). This election applies both as to new and *existing* property."[7]

Under the Senate version of the bill, therefore, Texas Gas would have been permitted to shift from liberalized depreciation with flow-through either to straight-line depreciation or, with the FPC's approval, to liberalized depreciation with normalization.

However, in conference, it was agreed that this right of election would be restricted to apply to post-1969 *expansion property only.* The Conference Report states:

> 1. *Depreciation allowed regulated industries (sec. 167 of the code)*
>
> The House bill provides that in the case of certain regulated industries (the furnishing or sale of . . . gas through a local distribution system, . . . and transportation of gas by pipeline) a taxpayer is *not permitted* to use accelerated depreciation *unless it "normalizes"* the current income tax reduction resulting from the use of such accelerated depreciation. . . .
>
> *This rule is not to apply in the case of a taxpayer that is at present flowing through the tax reduction to earnings for purposes of computing its allowable expenses on its regulated books of account.* Also, if the taxpayer is now using straight line depreciation as to any public utility property it may not change to accelerated depreciation as to that property.
>
> The Senate amendments make the following changes in the House bill: . . . (d) *an election is permitted to be made within 180 days after the date of enactment by a company at present on flowthrough to come under the rules of the bill;* . . .
>
> *The conference substitute (sec. 441 of the substitute and sec. 167(1) of the code) follows the Senate amendment except that the special provision referred to in*

[7] See note 6, *supra* (emphasis added).

(c) above is stricken and the 180-day election (item (d), above) is modified to apply to new property and not to replacement property. Even in the case of new property, however, the right to change over from the flowthrough method is to be available only to the extent the new property increases the productive or operational capacity of the company."[*]

Thus, Texas Gas is unable to invoke the election provision of Section 441(a) to abandon liberalized depreciation with flow-through with respect to its "existing" (including replacement) property for two reasons: first, since Texas Gas has been employing liberalized depreciation with flow-through, it is specifically prohibited, under the final version of the bill, from abandoning such depreciation (see the second paragraph of the Conference Report, *supra*); and, second, since the right of election was restricted to apply to post-1969 expansion property *only*, Texas Gas may not seek to circumvent this restriction by applying it to its pre-1970 and post-1969 *non*-expansion property—the subject of this set of cases (24,517 and 24,632).

What the Commission does by its decision in this set of cases, then, is to produce an effect precisely contrary to that envisioned by Congress in enacting the Tax Reform Act of 1969. This effect was considered by Congress in its deliberations on the appropriate scope for the right of election provided by Section 441(a), both in terms of its impact on rates and on tax revenues, and was specifically rejected. The Report of the House Committee on Ways and Means states:

> Consideration has been given to suggestions by the Federal Power Commission and others that regulated utilities no longer be permitted to use a method of depreciation other than straight line. However, your committee concluded that, in too many cases, this would place regulated utilities at an unfair competi-

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[*] See note 7, *supra* (emphasis added).

tive disadvantage, both in terms of the sale of their products or services and their attractiveness to equity investors. Also, this would result in prompt, substantial, and widespread utility rate increases.

Accordingly, your committee has determined in general to "freeze" the current situation regarding methods of depreciation in the case of those companies in what are, by and large, the more healthy utility industries."[50]

The Senate Report agreed with this perspective, stating in relevant part:

> Accordingly, the committee agrees with the House that it is *appropriate to in general* [sic] *'freeze' the current situation regarding methods of depreciation* in the case of those companies in what are, by and large, the more flourishing utility industries.[51]

The Senate Report, agreeing that a company using straight-line depreciation with normalization could not shift to flow-through under the bill, stated, with specific reference to utility companies such as Texas Gas which have been using liberalized depreciation with flow-through, "[o]ther companies—those that now flow through, as well as those in other regulated industries—are not limited by this general rule of the bill."[52]

Also, as the Summary of the Bill, prepared by the staffs of the Joint Committee on Internal Revenue Taxation and the Committee on Finance, observes with respect to the impact of Section 441(a) on revenues as well as rates:

> The bill substantially forestalls the entire revenue loss that the continuation of existing trends would have made almost inevitable. It does so in a way that (with very few exceptions) will require no increase in utility rates because of the tax laws, since

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[50] See note 26, *supra* (emphasis added).

[51] See note 6, *supra* (emphasis added).

[52] *Id.*, at 174.

by and large, it merely takes the various regulatory situations as it finds them and freezes those situations.[22]

There is nothing in the Tax Reform Act of 1969, then, which modifies the Commission's duty under the Natural Gas Act to require regulated utility companies such as Texas Gas, which had been using liberalized depreciation with flow-through with respect to their pre-1970 and post-1969 non-expansion property, to set rates which reflect actual expenditures alone with respect to such property. According to Congress, the only appropriate tax allowance for ratemaking purposes for a company such as Texas Gas, which has been using liberalized depreciation with flow-through with respect to its pre-1970 and post-1969 non-expansion property, is the income taxes actually paid.[23]

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[22] Summary of the Bill, prepared by the staff of the Joint Committee on Internal Revenue Taxation and the Committee on Finance, at 73.

[23] In a recent analogous case, the California Supreme Court held that Pacific Telephone and Telegraph Company's refusal, despite the fact that the California Public Utilities Commission was imputing accelerated depreciation with flow-through to those utilities which, like Pacific Telephone, used straight-line depreciation, to abandon straight-line depreciation (even though this meant a higher tax burden for Pacific Telephone in light of its expanding plant) [See pp. 4-5 of Slip Op.] was an "imprudent management decision" which it should not be permitted to pass on to its customers by means of higher rates. As the court there noted,

> . . . [I]t is clear that requiring ratepayers to put up the capital for the telephone system is contrary to the basic principle of utility rate setting. The basic principle is to establish a rate which will permit the utility to recover its cost and expenses plus a reasonable return on the value of property devoted to public use. . . . By permitting Pacific to include in its costs a charge for federal taxes greatly in excess of its actual federal tax ex-

B.

The FPC has argued that there is nothing in this Tax Reform Act indicating an intent on the part of Congress to alter the Commission's power to exercise its informed judgment as to what method of accounting can properly serve as the basis of ratemaking, and to weigh the cost to the consumer and the necessity to preserve a viable industry. The FPC urges that had Congress had such an intent, Congress would have manifested it by an amendment to the Natural Gas Act, not to a Revenue Act.

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pense, the Commission is deviating from this basic principle. We realize that the 1968 commission decision also deviated from the basic principle by refusing to permit Pacific to include in its costs all of its tax expense, but this deviation was based on Pacific's imprudent management.

It should also be pointed out that the effect of the instant decision [of the Commission below] is to reward Pacific for its imprudent management as compared to other utilities which prudently had adopted accelerated depreciation and flow-through prior to August 1969. Apparently, these utilities will continue to be required to flow-through the benefits of accelerated depreciation to the ratepayers, whereas Pacific will be allowed to use accelerated depreciation [under the Commission's decision below] without requiring flow-through, thus retaining most of the benefits for itself.

In the circumstances, we are satisfied that, in the light of Pacific's past imprudence, the commission could reasonably have ordered Pacific to continue the accounting practices established in the 1968 decision and that the commission abused its discretion in expressly *refusing to consider* imputed acceleration depreciation and flow-through as established in the 1968 decision.

City and County of San Francisco v. *Public Utilities Commission et al.*, S.F. 22794, & *Consumers Arise Now et al.* v. *Public Utilities Commission and Pacific Telephone and Telegraph Company*, S.F. 22793, pp. 15-16, Slip Op. (emphasis in original).

This overlooks the undeniable fact that methods of calculating depreciation are relevant both for taxation and ratemaking purposes. Congress here dealt with depreciation in the context of a revenue measure, but all its deliberations—particularly the committee reports of both houses, the conference committee report, and most significantly, the changes made in the bill at different stages—show its keen awareness of the measure's impact on the federal revenue, the natural gas industry, and the consumers. It may well be that some of the FPC's regulatory discretion has been lost by the enactment of this law; in effect, Congress has pondered the question, and has exercised what formerly was the FPC's perogative for it. The fact that Congress did so in the context of a Tax Reform Act cannot vitiate what Congress enacted.

To hold otherwise would be to rule that the carefully considered changes, granting an election to the company with respect to its expansion property but eliminating any choice by either company or FPC with respect to the company's *non-expansion property*,[24] were meaningless. The rule here urged by the FPC and Texas Gas is similar to that policy proposed by Chairman White, and this was rejected.[25] We here give effect to what Congress did; albeit cloaked in a revenue act, a statutory mandate in regard to the calculation of depreciation has an effect on the FPC's power to exercise its independent judgment as to what best will serve industry and consumers.

Our holding, however, should not be taken to mean that Section 441(a) of the Tax Reform Act of 1969 deprives the Commission in all cases of its discretion under the Natural Gas Act to permit utilities to abandon flow-through. There might be extraordinary circumstances in

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[24] See notes 3 and 23, *supra*.

[25] See note 26, *supra*.

which Section 441(a), taken in conjunction with the mandate of the Natural Gas Act, should not be construed to prevent the FPC in its underlying responsibility of protecting consumer interests from finding that those interests would be furthered by permitting the abandonment of flow-through. It is clear, however, that such consumer interests would not be furthered by permitting Texas Gas to abandon flow-through in the circumstances presented by the case at bar.

III.

Accordingly, the decision of the Federal Power Commission in its Orders No. 404 and 404-A with respect to the post-1969 *expansion* property of Texas Gas—the subject of cases no. 24,518 and 24,602—is affirmed. However, the action of the Commission in its Opinions No. 578 and 578-A and accompanying orders in regard to Texas Gas' pre-1970 and post-1969 *non*-expansion property—the subject of cases no. 24,517 and 24,632—is vacated and remanded to the Commission for action in accordance with this opinion.

SO ORDERED.

APPENDIX B

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S.App.D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 24,517

MEMPHIS LIGHT, GAS AND WATER DIVISION, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION
TENNESSEE VALLEY MUNICIPAL GAS ASSOC., ETC.,
INTERVENORS

No. 24,632

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK,
PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION, INTERVENOR

On Petitions for Rehearing

Filed May 11, 1972

Before FAHY, *Senior Circuit Judge*, and ROBINSON and WILKEY, *Circuit Judges*.

WILKEY, *Circuit Judge*: Petitions of the Federal Power Commission and Texas Gas Transmission Corporation, an intervenor, for rehearing and suggestions for rehearing *en banc*, of this court's action in vacating the order of the Commission with respect to Texas Gas' pre-1970 and post-1969 *non*-expansion property, focus on three main points:

1. Whether Congress' enactment of the 1969 Tax Reform Act limited the extent of the Commission's authority to permit regulated utilities such as Texas Gas to shift from accelerated depreciation with flow-through to similar depreciation with normalization with respect to their pre-1970 and post-1969 non-expansion property.

2. The import of the explanation of Section 441(a) of the 1969 Tax Reform Act in regard to point 1, *supra*, provided by the Staff of the Joint Committee on Internal Revenue Taxation.

3. The court's caveat, at the end of its opinion, with respect to the effect of Section 441(a) of the Act on the Commission's discretion to permit regulated utilities such as Texas Gas to abandon flow-through.

We deny the petitions for rehearing, as we find the Commission's and Texas Gas' arguments unpersuasive. Since both manifest some confusion over the meaning of our opinion and what we deem the proper interpretation of the statute involved, we set forth these additional views on the specific points raised in an effort at clarification for the responsible regulatory agency and the industry involved.

I. *The Extent of the Commission's Authority under Section 441(a) of the 1969 Tax Reform Act re Non-Expansion Property*

The Commission and Texas Gas return to the initial

House version of Section 441(a) of the 1969 Tax Reform Act to support their contention that Section 441(a), as finally enacted, did not curtail the Commission's discretion, with respect to pre-1970 and post-1969 *non*-expansion (existing or replacement) property, to permit regulated utilities such as Texas Gas to shift from accelerated depreciation with flow-through to similar depreciation with normalization. They point out (we do not disagree, see first full paragraph of text, page 16 of Slip Op.) that the House version would have permitted Texas Gas, with the Commission's approval, to shift from flow-through to normalization with respect to its pre-1970 and post-1969 non-expansion (as well as its post-1969 expansion) property.

It is at the Senate stage of the proceedings that our views diverge. Texas Gas and the Commission argue that the FPC's discretion to permit a regulated utility such as Texas Gas to shift its depreciation treatment of *non*-expansion property survived through both the Senate and Conference Committee versions of the legislation. Their interpretation is that subsequent versions reflect *additional* provisions (*e.g.*, the 180-day period during which the company may elect to change its method of depreciation) rather than *substitute* provisions which eventually made up the final bill. We think our analysis (pp. 15-18, Slip Op.) of the changes at different stages of the legislation makes clear why this contention is not valid, but for greater clarity we shall chart the transformations as the Tax Reform Act progressed through the legislative stages (see page 4).

Thus, between the initial House and Senate versions of Section 441(a), two differences emerge with respect to Situation III and to shifting from flow-through: First, under the Senate version, in contrast to the House, FPC approval is *not* required to shift from the flow-through to the straight-line method; and, second, the Senate limited (the Commission and Texas Gas can point to no

House Version Reckoned Three Possible Present Situations as both expansion and non-expansion Prop-erty Depreciation	*House Version Proposed Three Permissible Changes, with No Time Limit re Changes*	*Senate Version Reckoned Same Three Present Situations, but (1) Created Under III A Difference in Agency Approval Required; and (2) Limited Either Change to a 180-Day Election Period*	*Conference Committee Version*
I. Straight-line	None allowed	(Same)	(Same)
II. Normalization	To straight-line, or continue normalization, *without* agency approval (could not change to flow-through)	(Same)	(Same)
III. Flow-through	Continue flow-through, unless change to Straight-line, *with* agency approval; or Normalization, *with* agency approval	Continue flow-through, unless change to A. Straight-line, *without* agency approval; or B. Normalization, *but only with* agency approval. Either change to be elected within 180 days.	Same as Senate, but *modified* to make the 180-day election (item (3) in Conf. Rep.) apply to only (post-1969) property only, and available only to extent public utility capacity increased.

* For legislative history supporting this analysis, see: H.R. Rep. No. 413 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 131-134 (1969); S. Rep. No. 552 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 171-176 (1969); Conf. Rep. No. 782, 91st. Cong., 1st Sess. 312-313 (1969).

language to the contrary) *all* changes re both expansion and non-expansion property to a 180-day election period. In view of these differences, the Conference Committee was free to modify the House and Senate versions in an attempt to resolve them.[1] Neither Texas Gas nor the Commission dispute the power of the conferees to make the second change, to curtail the 180-day election provision so as to apply *only* to post-1969 expansion property.

As to the first change, there was clearly a disagreement between the Senate and the House over the right of a regulated utility to shift from accelerated depreciation with flow-through to straight-line depreciation, with or without agency approval. This disagreement entitled the conferees (1) to choose the Senate version, limiting all shifting from the flow-through method to a 180-day period, *and (2) to make it applicable to post-1969 expansion property only.* Clearly, such an option is a "germane modification of subjects in disagreement"—here the permissible extent of abandonment of accelerated depreciation with flow-through.

The variety and extent of differences between the two versions was acknowledged by the Staff of the Joint Committee on Internal Revenue Taxation,[2] a source much

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[1] Section 136 of the Legislative Reorganization Act of 1946, 2 U.S.C. § 190(c)(a), provides in pertinent part:

> (a) In any case in which a disagreement to an amendment in the nature of a substitute has been referred to conferees, it shall be in order for the conferees to report a substitute on the same subject matter; but they may not include in the report matter not committed to them by either House. *They may, however, include in their report in any such case matter which is a germane modification of subjects in disagreement* (emphasis supplied).

[2] As stated in the Letter of Transmittal in their *General Explanation of the Tax Reform Act of 1969, H.R. 13270, 91st Congress, Public Law 91-172* (3 December 1970).

relied upon here by the Commission and Texas Gas: "The Tax Reform Act of 1969, because of its comprehensive scope and because of the *many changes* which were made in this legislation, both by the Senate and *subsequently by the conferees*, is an illustration where the differences [between the versions of each House] were especially significant."[3]

In permitting a taxpayer such as Texas Gas to shift from accelerated depreciation with flow-through to straight-line depreciation with or without the appropriate agency's approval, the Senate was no doubt interested in increasing governmental revenues (since under flow-through the tax reduction is passed on to the utility's customers). The House, however, by limiting changes from flow-through either to straight-line or normalization *only with* agency approval, was reflecting the concern that emphasis on a shift to straight-line depreciation, as expressed by the Senate version, would place taxpayers such as Texas Gas at a competitive disadvantage, both as to the sale of their products or services and as to their attractiveness to equity investors.[4]

Thus, the conferees' resolution of this disagreement in favor of the latter concern by limiting the extent to which regulated utilities may abandon flow-through reflects Congress' overall intent "in general to 'freeze' the current situation regarding methods of depreciation in the case of those companies in what are, by and large, the more healthy utility industries."[5] And, as both the House and

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[3] At p. 111 (emphasis added).

[4] H.R. Rep. No. 413 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 132 (1969).

[5] *Id.*, at 133; *see also*, to the same overall effect, S. Rep. No. 552 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 172 (1969), which states: "Accordingly, the committee agrees with the House that it is appropriate to in general [sic]

Senate Reports indicate, "About half the regulatory agencies require utilities that use accelerated depreciation for tax purposes to 'flow through' the resulting reduction in Federal income taxes currently to the utilities' customers. . . . Some agencies insist that utilities subject to their jurisdiction use accelerated depreciation for tax purposes; even if those utilities use straight line depreciation for tax purposes, such agencies treat them for ratemaking purposes as though they had reduced their Federal income tax expense by using accelerated depreciation."[6]

This overall congressional objective to forestall prospective revenue losses, without handicapping the utility industry, was a prime consideration at all stages of the legislation. In focusing on the specific language of the House version of the bill, Texas Gas and the Commission give no notice to this overall objective, the weight it had at all stages, and how the final conferees' changes reflect this, although we stressed this in our opinion (pp. 18-20, Slip Op.).

II. *Import of the General Explanation by the Staff of the Joint Committee on Internal Revenue Taxation.*

Reliance by the Commission and Texas Gas on one specifically cited portion of the *General Explanation of the Tax Reform Act of 1969, H.R. 13270, 91st Congress, Public Law 91-172*, prepared by the Staff of the Joint Committee on Internal Revenue Taxation (3 December 1970), for support for the proposition that Section 441(a) of the Act as finally enacted did not diminish the Commission's authority to permit a taxpayer such as Texas Gas from abandoning flow-through with respect to its

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'freeze' the current situation regarding methods of depreciation in the case of those companies in what are, by and large, the more flourishing utility industries."

[6] H.R. Rep. No. 413, at 131-132; S. Rep. No. 552, at 171-172.

pre-1970 and post-1969 non-expansion property is mistaken. We are cited to page 151 of the *General Explanation*, to wit:

> More specifically, in the case of *existing* property the following rules apply:
>
> * * * *
>
> (3) If the taxpayer was taking accelerated depreciation and flowing through to its customers the benefits of the deferred taxes as of August 1, 1969, then the taxpayer would continue to do so *(except for a special election procedure discussed below)*, unless the appropriate regulatory agency permits a change as to that property. *That is, the Act does not require the taxpayer to flow through, but it also does not affect any power the regulatory agency might have to require the taxpayer to flow through.* (Emphasis supplied.)

The first revealing aspect of this language is that all of it except the italicized portions (which were added by the Staff) was lifted, with only minor modifications, from the House and Senate Reports,[1] both of which were com-

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[1] The House Report describes the House Bill:

> (3) If the taxpayer is taking accelerated depreciation and is flowing through to its customers the benefits of the deferred taxes, then the taxpayer must continue to do so, unless the appropriate regulatory agency permits a change as to that property.

H.R. Rep. No. 413 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 123 (1969).

The Senate Report in turn describes the House Bill:

> (3) If the taxpayer is taking accelerated depreciation and flowing through to its customers the benefits of the deferred taxes, then the taxpayer would continue to do so (except as provided under the committee amendments which are discussed below), unless the appropriate regulatory agency permits a change as to that property.

S. Rep. No. 552 [To Accompany H.R. 13270], 91st Cong., 1st Sess. 178 (1969).

meeting on the initial House version of Section 441(a). For the Commission and Texas Gas, then, to point to this language as determinative of Congress' *final* intent in enacting Section 441(a) of the Act is unavailing. At best, this language is confusing and uncertain; it cannot carry the meaning ascribed to it by the Commission and Texas Gas, particularly in view of the following page 152, discussed *supra*. Significantly, there is no mention of such continued Commission authority in this particular respect in the Conference Committee Report, an omission reflecting the conferees' resolution of the differences between the two initial versions of Section 441(a).

Furthermore, as we have seen by the provisions discussed and displayed in the chart, *supra*, there never was at any time in any version of the House, Senate, or conference, a power in the agency to compel or permit a company to change from any method of depreciation accounting to flow-through. To have included such a provision would have been directly contrary to the overall objective of this portion of the Act—"in general to 'freeze' the current situation regarding methods of depreciation." (As discussed pp. 18-20, Slip Op.) After the Tax Reform Act of 1969, the permissible shifts were contemplated to be *away from* flow-through, at the company's option, with changed requirements as to agency approval and time (see chart, *supra*).

Finally, the comfort Texas Gas and the Commission derive from page 151 is taken away by page 152 of the *General Explanation*, not cited to us. There we find:

> The Act permits an election to be made within 180 days after the date of enactment of the Act—i.e., by June 28, 1970—for a utility in one of the regulated industries covered by this provision to shift from the flow-through to the straight line method, with or without the permission of the appropriate regulatory agency, or to permit it with the permission of the regulatory

agency to shift to the normalization method, that is, to come under general rules of the Act.

This election applies to new property, but only to the extent it increases the taxpayer's capacity . . ."[1]

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[1] Staff of the Joint Committee on Internal Revenue Taxation, *General Explanation of the Tax Reform Act of 1969, H.R. 13270, 91st Congress, Public Law 91-172*, 182 (2 December 1970). The language of the statute, as it is codified, reflects the fact that a utility's election to shift from flow-through to a different method of depreciation is applicable only to new expansion property:

(1) Reasonable allowance in case of property of certain utilities.—

(1) *Pre-1970 public utility property.*

(2) *Post-1969 public utility property.*—In the case of any post-1969 public utility property, the term "reasonable allowance" as used in subsection (a) means an allowance computed under—

(A) a subsection (1) method,

(B) a method otherwise allowable under this section if the taxpayer uses a normalization method of accounting, or

(C) the applicable 1969 method, if, with respect to its pre-1970 public utility property of the same (or similar) kind most recently placed in service, the taxpayer used a flow-through method of accounting for its July 1969 accounting period.

(4) *Special rules as to flow-through method.—*

(A) *Election as to new property representing growth in capacity.*—If the taxpayer makes an election under this subparagraph within 180 days after the date of the enactment of this subparagraph in the manner prescribed by the Secretary or his delegate, in the case of taxable years beginning after December 31, 1970, paragraph (2) (C) shall not apply with respect to any post-1969 public utility property, to the extent that such property constitutes property which increases the productive or operational capacity of the taxpayer

Here we have set forth the rule—and the rationale therefor—of the final version of the statute. "Utilities on flow-through could elect" to change to either straight-line depreciation or accelerated depreciation with normalization within 180 days after enactment of the Act, but—"This election applies to new property, but only to the extent it increases the taxpayer's capacity."

There is nothing about old, existing, non-expansion property which "increases the taxpayer's capacity." Only new, expansion property could do so. Hence, if we bear in mind the congressional intent generally "to freeze" the present depreciation situation, it appears logical that the permissible shift in accounting practices would be limited, and that an exception might logically be made for new expansion property increasing productive capacity, at taxpayer option, and with agency approval required if the shift is to normalization. If we take Texas Gas' and the Commission's evaluation of the words on page 151—and ignore page 152 completely—then the exception is for all property and swallows up the whole, thus vitiating any congressional intent "to freeze" generally depreciation accounting practices for utilities. Texas Gas and the FPC continually urge that there are no words in this Tax Reform Act saying specifically that the Power Commission's discretion is curtailed, an argument which, to our minds, simply misses the purpose of this portion of the Act. The objectives in regard to a general freeze, in regard to balancing pro-

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with respect to the goods or services described in paragraph (8)(A) and does not represent the replacement of existing capacity.

Int. Rev. Code of 1954, § 167(1), *as amended* 1969.

While some may see differently, we suggest that the intent of Congress is not readily apparent on the plain face of this statute; hence our resort to its legislative history.

spective revenue loss against possible impairment of the utilities' ability to raise capital and service customers at low rates, all would have been difficult to achieve without placing the resulting limitation on the Commission's discretion. This the language of the Tax Reform Act necessarily did, and to hold otherwise would be to undo what was most carefully done.

III. *The Court's Caveat with Respect to the Effect of Section 441(a)*

Finally, the Commission asserts that the court's opinion is misleading in that "On the one hand, this Court finds that the Commission lost its discretion to allow Texas Gas to switch from flow-through. Yet this Court holds that the Commission has discretion to permit abandonment of flow-through in 'extraordinary circumstances.'" (Commission brief, p. 13, n. 6.)

The Commission fails to read the court's language with care. What we stated is that "There *might be* extraordinary circumstances in which Section 441(a), taken in conjunction with the mandate of the Natural Gas Act, should not be construed to prevent the FPC in its underlying responsibility to protecting consumer interests from finding that those interests would be furthered by permitting the abandonment of flow-through." [Slip Op., pp. 22-23 (emphasis supplied).] Clearly, the court's language indicates simply the possibility that such circumstances might exist; it does not state that they do. For the Commission to assume otherwise is to ignore the plain meaning of the court's language. What the court intended here was merely to leave open the possibility that such circumstances might exist, rather than to assume categorically that they do not.

IV. *Conclusion*

For the reasons stated above, the petitions of the Commission and Texas Gas for rehearing are

Denied.

APPENDIX C

United States Court of Appeals for the District of Columbia Circuit

September Term, 1971

No. 24,517

MEMPHIS LIGHT, GAS AND WATER DIVISION, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION, TENNESSEE VALLEY MUNICIPAL GAS ASSOCIATION, ETC., INTERVENORS

No. 24,632

PUBLIC SERVICE COMMISSION OF THE STATE OF NEW YORK, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

TEXAS GAS TRANSMISSION CORPORATION, INTERVENOR

Petitions for Review of Orders of the Federal Power Commission

Before: FAHY, *Senior Circuit Judge*, and ROBINSON and WILKEY, *Circuit Judges*.

JUDGMENT

These cases came on to be heard on the record from the Federal Power Commission, and were argued by Counsel. Upon consideration thereof, it is

ORDERED AND ADJUDGED by this Court that orders of the Federal Power Commission on review herein are hereby vacated, and these cases are hereby remanded to the Federal Power Commission for action in accordance with the opinion of this Court filed herein this date.

A true copy:

NATHAN J. PAULSON,
Clerk.

DOROTHY E. LONG,
Deputy Clerk.

Dated: February 18, 1972.

Opinion by Circuit Judge Wilkey.

APPENDIX D

United States of America, Federal Power Commission

ACCOUNT 282; LIBERALIZED DEPRECIATION; FLOW-THROUGH; ACCUMULATED DEFERRED TAXES; NORMALIZATION

Before Commissioners: JOHN N. NASSIKAS, *Chairman*; LAWRENCE J. O'CONNOR, JR., CARL E. BAGGE, JOHN A. CARVER, JR., and ALBERT B. BROOKE, JR.

Docket Nos. RP69-41, RP70-14

TEXAS GAS TRANSMISSION CORPORATION

Opinion No. 578

OPINION AND ORDER GRANTING PERMISSION TO USE LIBERALIZED DEPRECIATION WITH NORMALIZATION FOR ACCOUNTING AND RATE PURPOSES

(Issued June 3, 1970)

NASSIKAS, *Chairman*:

1. The rate and accounting issues with respect to the property of Texas Gas Transmission Corporation on which liberalized depreciation is now being taken with flow-through of benefits are now before the Commission while other issues in this proceeding are subject to settlement negotiations. The proceedings commenced with the filing of a rate increase by Texas Gas on June 27, 1969, in Docket No. RP69-41, which

was suspended until January 12, 1970; a further rate increase was filed on November 7, 1969, in Docket No. RP70-14 to track a rate increase filed by its supplier, United Gas Pipeline Company, and this was suspended until May 16, 1970.

2. At the hearing the proceeding was divided into two phases by the Presiding Examiner with Phase I comprising questions of rate of return, associated income taxes, and reversion to straight-line depreciation. On motion of Staff Counsel the Commission omitted the intermediate decision with respect to Phase I issues, and briefs were filed by a number of parties. Lately settlement negotiations have been held among the parties and the Commission Staff with respect to both Phase I and Phase II issues, but the issues relating to liberalized depreciation have been left for determination by the Commission. On May 4, 1970, Texas Gas filed a motion for an expedited decision on the tax depreciation issue alleging that under the Tax Reform Act of 1969, 83 Stat. 487, it would have to make an election with respect to certain "post-1969" property on or before June 29, 1970, and requesting oral argument. An answer to the motion was filed by the City of Hamilton, Ohio, contesting some of Texas Gas' arguments, agreeing that the case should be resolved without any further delay, and also asking for oral argument.

3. Texas Gas now employs liberalized depreciation under Section 167 of the Internal Revenue Code and flows through the benefits to its customers. It alleges that it did not make an election to utilize liberalized depreciation until the Commission had issued a declaratory order that it would permit companies subject to its jurisdiction to normalize taxes for both accounting and ratemaking purposes. *Amere Gas Utilities Co.*, 15 FPC 760 (1956). Under this normalization tech-

sique, Texas Gas computed its tax allowance for rate-making purposes as though it were using straight-line depreciation, but used liberalized depreciation for computing the amount of taxes actually paid. The difference between taxes collected through its rates and taxes actually paid was credited to Account 282, Accumulated Deferred Income Taxes—Liberalized Depreciation.

4. In *Alabama-Tennessee Natural Gas Company*, 31 FPC 308, 923 (1964), aff'd 359 F. 2d 318 (5th Cir. 1966), cert. *denied* 385 U.S. 847 (1966), we required that the tax benefits of liberalized depreciation be flowed-through to consumers. Texas Gas, for the reasons discussed below, now proposes to abandon flow-through for accounting and ratemaking purposes. For post-1969 property representing an expansion it proposes to effect this by an election under the Tax Reform Act and has shown a preference to utilize liberalized depreciation with normalization. For pre-1970 property, and presumably any other property not subject to the election, it now states by letter dated May 22, 1970, served on all the parties that:

> This letter is being written in order to make it perfectly clear that Texas Gas proposes to use a normalized method of accounting with respect to pre-1970 public utility property if the Commission permits Texas Gas to use normalization for rate-making purposes. Alternatively, Texas Gas proposes to revert to a straight-line method of computing tax depreciation with respect to pre-1970 public utility property, if the Commission permits the associated taxes to be included in Texas Gas' cost of service. Of the two methods, Texas Gas prefers the normalization method.

5. The Tax Reform Act (Section 441 amending Section 167 of the Internal Revenue Code) divides

utility property into pre-1970 property (that which was utility property in the hands of any person at any time before January 1, 1970) and post-1969 property (that which is not pre-1970 property). A taxpayer, like Texas Gas, using the flow-through method of accounting may with respect to post-1969 property elect to change to straight-line depreciation, or with our permission to the normalization method, to the extent the property increases the productive or operational capacity of the taxpayer and does not represent the replacement of existing capacity. Contrary to some of the arguments expressed in the briefs, it is clear that Congress intended this election to apply for rate making purposes as well as tax purposes.

6. The Senate Report[1] states that where the election is made "the agency would not be able to impute the use of accelerated depreciation with flow-through"; and the House Report[2] states "the taxpayer will be permitted to elect straight line depreciation as to such new property and, if the taxpayer seeks to use accelerated depreciation, the regulatory agency will be permitted to in effect force the taxpayer to straight line depreciation by not permitting normalization. The regulatory agency will not, in such cases, be permitted to require flow through of deferred taxes." It is true, as the City of Hamilton points out, that the House Committee rejected the suggestion that utilities be required to revert to straight line depreciation and stated that it intended to "freeze" the current situation regarding methods of depreciation in order to avoid putting the companies at a competitive disadvantage or inducing widespread rate increases, but this was the general policy and a specific exception was made for an elec-

[1] Senate Report No. 91-552 on H.R. 13270, pp. 173-174.
[2] House Report No. 91-413 on H.R. 13270, p. 133.

...with respect to post-1969 property where the companies wished to depart from the flow-through method.

7. Referring to these provisions of the Tax Reform Act in our Order No. 404, Statement of Policy, issued May 15, 1970, we determined that it was in the public interest, as to property as to which the election is made, "that electric and natural gas pipeline companies regulated by the Commission be permitted to employ a normalization method in their accounts and annual reports, as well as for ratemaking purposes," but we did not decide the ratemaking or accounting issues with respect to other property such as that constructed or acquired prior to January 1, 1970, on which flow-through is being used. Therefore in this proceeding if Texas Gas elects to abandon flow-through on post-1969 property, it is permitted to employ normalization for accounting and ratemaking purposes, but there still must be determined the question whether it may abandon flow-through and use liberalized depreciation with normalization for property not subject to the election, that is the pre-1970 property and the post-1969 property which does not represent an expansion. Under the Tax Reform Act our authority to determine whether a company may elect such a change is not diminished.[1]

8. In our opinion Texas Gas has shown good reason to abandon flow-through for accounting and ratemaking purposes. In *Alabama-Tennessee*, we based our conclusions on our finding that liberalized depreciation would exceed straight-line depreciation where the company continues to make capital additions. Even where the composite plant of a company remains stable, we found, annual liberalized depreciation would

[1] House Report No. 91-413, U.S. Code Congressional and Administrative News, p. A-141.

not be lower than straight line depreciation. Thus we concluded that a regulated utility would never be required to pay higher income taxes because of its election to obtain liberalized depreciation unless its gross plant declines in dollar value as a result of lower demand or lower plant construction costs. In support of this approach we noted that almost all responsible forecasts reflected the widespread belief that the gas pipeline industry would continue to expand at least until 1980, and we concluded that the pattern of growth in demand and plant capacity with respect to Alabama-Tennessee and the gas pipeline industry generally would continue for the reasonably foreseeable future. We followed the same approach in *Midwestern Gas Transmission Co.*, 36 FPC 61 (1961), aff'd 298 F. 2d 444 (7th Cir.), *cert. denied*, 369 U.S. 808 (1962). It should be observed that while we were upheld in requiring flow-through in both these cases, the court in neither case indicated that we are required to order that the companies use flow-through.

11 Under the present circumstances the considerations applicable in *Alabama-Tennessee* and *Midwestern* do not obtain. By reason of Texas Gas' proposed election under the Tax Reform Act and Order No. 404, depreciation on the facilities, constructed after the beginning of 1970 which increase its capacity, will be subject to normalization rather than flow-through. Therefore tax depreciation on such new facilities will not be available to offset the declining tax depreciation deductions on the older facilities as contemplated in the *Alabama-Tennessee* and *Midwestern* cases.

12 Excluding new expansion facilities from consideration, the continued use of liberalized depreciation on the pre-1970 plant will not create a tax saving. It is not an answer to urge that the allowable

tax depreciation of the pipeline plant remaining after addition of the post-1969 expansion facilities will be sufficiently stable to avoid forever repayment of taxes earlier avoided by liberalized depreciation. This is because the permissible tax depreciation life of natural gas properties is much shorter than the physical life of such properties. In other words, the period of time over which the properties would be useful and depreciable for tax purposes is dependent on the gas supply rather than the useful physical life of the plant. It therefore follows that the pre-1970 tax plant will not be a stable plant in the sense that plant retirements are replaced by new facilities, but the basis of tax depreciation related thereto will decline, so that there is little chance with respect to this plant that there will be any permanent tax savings. Under these circumstances, therefore, Texas Gas is correct in contending that normalization in computing the tax allowance for rate purposes with respect to its pre-1970 facilities offers more hope for stability of rates for its customers and more assurance that the company can earn its fair rate of return without future rate increases. Further benefits of normalization are that it will improve the company's before tax coverage of interest, thereby enhancing the quality of its securities, and that it will help alleviate present heavy cash shortages.

11. While, of course, Texas Gas is subject to regulation and is required to operate with all reasonable economies,' here it would appear that a reversion to normalization with respect to the pre-1970 properties (and post-1969 properties not subject to the election) would lead to more stable tax costs in the long run insofar as its customers are concerned. It is likely that

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[illegible] *El Paso Natural Gas Co. v. F.P.C.*, 281 F.2d 567 (5th Cir. 1960), *cert. denied*, 366 U.S. 912 (1961).

not be lower than straight-line depreciation. Thus we concluded that a regulated utility would never be required to pay higher income taxes because of its election to claim liberalized depreciation unless its gross plant declines in dollar value as a result of lower demand or lower plant construction costs. In support of this approach we noted that almost all responsible forecasts reflected the widespread belief that the gas pipeline industry would continue to expand at least until 1980, and we concluded that the pattern of growth in demand and plant capacity with respect to Alabama-Tennessee and the gas pipeline industry generally would continue for the reasonably foreseeable future. We followed the same approach in *Midwestern Gas Transmission Co.*, 36 FPC 61 (1961), aff'd 388 F. 2d 444 (7th Cir.), *cert. denied*, 392 U.S. 923 (1968). It should be observed that while we were upheld in requiring flow-through in both these cases, the court in neither case indicated that we are required to order that the companies use flow-through.

9. Under the present circumstances the considerations applicable in *Alabama-Tennessee* and *Midwestern* do not obtain. By reason of Texas Gas' proposed election under the Tax Reform Act and Order No. 484, depreciation on its facilities, constructed after the beginning of 1970 which increase its capacity, will be subject to normalization rather than flow-through. Therefore tax depreciation on such new facilities will not be available to offset the declining tax depreciation deductions on the older facilities as contemplated in the *Alabama-Tennessee* and *Midwestern* cases.

10. Excluding new expansion facilities from consideration, the continued use of liberalized depreciation on the pre-1970 plant will not create a tax saving. It is not an answer to urge that the allowable

tax depreciation of the pipeline plant remaining after retirement of the post-1969 expansion facilities will be sufficiently stable to avoid forever repayment of taxes earlier avoided by liberalized depreciation. This is because the permissible tax depreciation life of natural gas properties is much shorter than the physical life of such properties. In other words, the period of time over which the properties would be useful and depreciable for tax purposes is dependent on the gas supply rather than the useful physical life of the plant. It therefore follows that the pre-1970 tax plant will not be a stable plant in the sense that plant retirements are replaced by new facilities, but the basis of tax depreciation related thereto will decline, so that there is little chance with respect to this plant that there will be any permanent tax savings. Under these circumstances, therefore, Texas Gas is correct in contending that normalization in computing the tax allowance for rate purposes with respect to its pre-1970 facilities offers more hope for stability of rates for its customers and more assurance that the company can earn its fair rate of return without future rate increases. Further benefits of normalization are that it will improve the company's before tax coverage of interest, thereby enhancing the quality of its securities, and that it will help alleviate present day cash shortages.

11. While, of course, Texas Gas is subject to regulation and is required to operate with all reasonable economies,[4] here it would appear that a reversion to normalization with respect to the pre-1970 properties (and post-1969 properties not subject to the election) would lead to more stable tax costs in the long run as far as its customers are concerned. It is likely that

[4] *See El Paso Natural Gas Co. v. F.P.C.*, 281 F.2d 567 (5th Cir. 1960), *cert. denied*, 366 U.S. 912 (1961).

tax costs under the flow-through method, while lower at this time than they would be under normalization, could increase in the future, putting financial pressure on the company and creating the need for increased rates. Under these conditions, the company's management is in the best position to examine and pass judgment on these effects, and we are prepared to respect the exercise of managerial discretion at least to the extent of permitting Texas Gas to adopt liberalized depreciation with normalization. Furthermore, upon re-examination of the basis of our *Alabama-Tennessee* and *Midwestern* decisions in the light of the Tax Reform Act of 1969, particularly its effect on post-1969 property, and the impact of the tax law on pipeline property, the findings made in those two cases are no longer applicable, and accordingly the cases are overruled to the extent they are inconsistent with this decision.

12. In reply to the arguments and evidence of Texas Gas on the effect of continuing liberalized depreciation and flow-through, Memphis presents an exhibit which purports to show that even if gross plant leveled off and then declined the use of liberalized depreciation would not require a rate increase, because the decline in return and related income tax would more than counterbalance any increase in tax resulting from lower deductions under liberalized depreciation. With comparable result, the Staff assumes an initial investment with no additions or retirements and shows that in the early years that the property is in service, as tax deductions decline, the advantage to consumers of using liberalized depreciation with flow-through declines until it becomes negative, but this tendency is offset by a tax reduction due to the decline in the rate base. In our opinion, the effect of the declining rate base should not be used to offset the

effects of liberalized depreciation with flow-through. Where there is no new investment the rate base declines in any case, regardless of the method of tax depreciation. While Texas Gas' pre-1970 properties may represent a declining net investment, the company will undoubtedly be adding to its entire rate base by post-1969 construction, and its operating expenses may well be increasing. Therefore, if Texas Gas remains on flow-through it appears that it may be benefitting present consumers at the unwarranted expense of future consumers. On the other hand, there appears to be little possibility that if Texas Gas chooses to use normalization on its pre-1970 property it will be providing for decreased rates to consumers in later years at the expense of present consumers.

13. To conclude, we shall grant approval to Texas Gas to exercise its discretion to abandon flow-through with respect to the pre-1970 property and post-1969 non-expansion property and to adopt liberalized depreciation with normalization with respect to this property. Texas Gas, through its election under the Tax Reform Act, already has permission to use liberalized depreciation with normalization with respect to its post-1969 expansion property. Balances in Account 282 should continue to be deducted from the rate base in computing cost of service for ratemaking purposes.

14. Because the issues have been well covered in the briefs we do not think that oral argument is necessary.

The Commission orders:

(A) In the computation of its Federal Income Tax allowance for ratemaking purposes as well as for accounting purposes, Texas Gas is permitted to use liberalized depreciation with normalization with respect to its property other than that subject to election under Section 167(1)(4)(A) of the Internal Revenue Code as amended by Section 441 of the Tax

Reform Act of 1969. Such election applies to property constructed or acquired on or after January 1, 1970, to the extent it increases the productive or operational capacity of the company and does not represent the replacement of existing capacity. Texas Gas may reflect any such change in its rates, as well as any change in costs arising from its proposed election. In computing its cost of service for ratemaking purposes balances in Account 282 should continue to be deducted from the rate base.

(B) Oral argument is denied.

By the Commission:

[SEAL] GORDON M. GRANT,
Secretary.

APPENDIX E

United States of America, Federal Power Commission

ACCOUNT 282; LIBERALIZATION DEPRECIATION; FLOW-THROUGH; ACCUMULATED DEFERRED TAXES; NORMALIZATION; PRACTICE AND PROCEDURE (DUE PROCESS)

Before Commissioners: JOHN N. NASSIKAS, *Chairman*; LAWRENCE J. O'CONNOR, Jr., CARL E. BAGGE, JOHN A. CARVER, Jr., and ALBERT B. BROOKE, Jr.

Docket Nos. RP69-41, RP70-14

TEXAS GAS TRANSMISSION CORPORATION

Opinion No. 578-A

OPINION AND ORDER DENYING REHEARING

(Issued July 21, 1970)

NASSIKAS, *Chairman*:

1. The Memphis Light, Gas & Water Division (Memphis) on June 29, 1970, the Public Service Commission of the State of New York (New York) on July 2, 1970, and the Philadelphia Gas Works Division of UGI Corporation (PGW) on July 6, 1970,[1] have filed applications for rehearing with respect to our Opinion No. 578 and order issued June 3, 1970, in the above-entitled proceeding. In Opinion No. 578 and order we permitted Texas Gas Transmission Corporation to use liberalized depreciation with normalization

[1] July 3, 4, and 5, 1970, were United States Government holidays.

with respect to property other than its post-1969 property, which is subject to election under Section 441 of the Tax Reform Act of 1969, 83 Stat. 487, to abandon use of liberalized depreciation for tax purposes. Under our Order No. 404, Statement of Policy, issued May 15, 1970, instead of reverting to straight-line depreciation the electric or natural gas pipeline company making the election is permitted to employ the normalization method for accounting as well as ratemaking. In most cases the points made on rehearing have been considered in Opinion No. 578, and any further discussion would be superfluous, but in other cases additional comments, in our opinion, would indicate more clearly the basis of our opinion.

2. Memphis and New York contend that we deprived them of due process of law in permitting Texas Gas to adopt liberalized depreciation with normalization for the non-elective properties. New York says the sole depreciation issue was whether Texas Gas should be granted permission to abandon liberalized depreciation with flow-through in order to change to straight-line depreciation for tax purposes. The Presiding Examiner provided that the hearing should be phased in accordance with our order of August 11, 1969, 42 FPC 511. He stated that "In Phase I the issues of rate of return and related income tax will be tried, and the issue of the return from accelerated to straight-line depreciation, insofar as the principle thereof is involved" (Tr. 69-70). The Tax Reform Act and our Order No. 404 dealt with the property subject to election. With respect to the property not subject to election it seems clear that, if properly supported by the record, we could deny Texas Gas' request to depart from liberalized depreciation, or we could grant it. We could also prescribe other solutions to the problem. In this instance the use by Texas

of liberalized depreciation with normalization, while it increases the tax costs to its customers, has some advantages over a reversion to straight-line depreciation for tax purposes. Normalization, as our opinion indicates, would improve the company's cash position, would, in effect, provide it with an interest free fund, and, because of the deduction of the accumulated reserves in Account 282 from the rate base, would reduce the company's cost of service and benefit consumers. This is a solution which we find more in the public interest than reversion to straight-line depreciation, and we could have treated Texas Gas for ratemaking purposes as though it were following this course. Compare *Midwestern Gas Transmission Co.*, 25 FPC 61 (1961), aff'd 388 F.2d 444 (7th Cir.), *cert. denied* 392 U.S. 928 (1968). Therefore the letter from counsel for Texas Gas dated May 22, 1970, which we quote in our original opinion, does not change the nature of the proceedings or introduce a new issue. It merely shows that the company does not oppose the solution which we find preferable.

3. New York argues that there are relationships between the tax depreciation issue and the rate of return allowance, so that the Commission was not free to decide one of the issues without deciding the other. As explained in Opinion No. 578 the rate of return issue was subject to settlement negotiations which have now resulted in a settlement approved by the Commission. In that order it is pointed out that use of liberalized depreciation with normalization does not represent additional return to Texas Gas.

4. Memphis and New York also argue that we improperly founded our determination on management discretion. This was not our purpose. Because of the discretion authorized by the Tax Reform Act it is our opinion, as expressed in Opinion No. 578, that tax

costs under the flow-through method could increase in the future with undesirable rate consequences. While our findings and conclusions were supported by the judgment of management, we were not basing them on management discretion but on our own judgment of the facts and the law.

5. They argue, further, that the Tax Reform Act or its legislative history do not permit or require us to allow the use of liberalized depreciation with normalization. Section 441 of the Tax Reform Act, it is true, does not require a change from flow-through to normalization, but providing an election with respect to post-1969 property changes the economic conditions with respect to the use of flow-through on existing property. New York quotes the Conference Report[1] to the effect that a taxpayer is not permitted to use accelerated depreciation unless it uses normalization but that this rule does not apply to a taxpayer presently using flow-through. However, this is not inconsistent with our permitting a change from flow-through to normalization.

6. PGW argues similarly that the Tax Reform Act did not confer on us additional power to permit an abandonment of flow-through in the absence of a justifying change in factual circumstances unrelated to the effect of the Tax Reform Act. We see no reason why the impact of the Tax Reform Act may not be a circumstance that might militate in favor of permitting Texas Gas to abandon flow-through accounting. As already noted, the Tax Reform Act permits the company to abandon flow-through with respect to post-1969 elective property. This changes the effect of liberalized depreciation with flow-through on the Company and its customers. For the reasons set forth in Opinion No. 578 we accordingly permitted Texas

[1] Conference Report No. 91-782, U.S. Code Congressional and Administrative News, p. A-785.

Gas to abandon flow-through for ratemaking and accounting and employ normalization.

The Commission further finds:

The assignments of error and grounds for rehearing set forth in the above applications for rehearing and motions for stay present no facts or legal principles which would warrant any change in or modification of Opinion No. 578 and order of June 3, 1970.

The Commission orders:

The applications for rehearing filed by Memphis, New York and PGW are denied.

By the Commission:

[SEAL] GORDON M. GRANT,
Secretary.

APPENDIX F

STATUTE INVOLVED

Section 441 of the Tax Reform Act of 1969, 83 Stat. 625, 26 U.S.C. 167(*l*), provides:

(a) IN GENERAL. Section 167 (relating to depreciation) is amended by inserting after subsection (k) (added by section 521) the following new subsection:

"(l) REASONABLE ALLOWANCE IN CASE OF PROPERTY OF CERTAIN UTILITIES.—

"(1) PRE-1970 PUBLIC UTILITY PROPERTY.—

"(A) IN GENERAL.—In the case of any pre-1970 public utility property, the term 'reasonable allowance' as used in subsection (a) means an allowance computed under—

"(i) a subsection (l) method, or

"(ii) the applicable 1968 method for such property. Except as provided in subparagraph (B), clause (ii) shall apply only if the taxpayer uses a normalization method of accounting.

"(B) FLOW-THROUGH METHOD OF ACCOUNTING IN CERTAIN CASES.—In the case of any pre-1970 public utility property, the taxpayer may use the applicable 1968 method for such property if—

"(i) the taxpayer used a flow-through method of accounting for such property for its July 1969 accounting period, or

"(ii) the first accounting period with respect to such property is after the July 1969 accounting period, and the taxpayer used a flow-through method of accounting for its July 1969 accounting period for the property on the basis of which the applicable 1968 method for the property in question is established.

"(2) POST-1969 PUBLIC UTILITY PROPERTY.—In the case of any post-1969 public utility property, the term 'reasonable allowance' as used in subsection (a) means an allowance computed under—

"(A) a subsection (l) method,

"(B) a method otherwise allowable under this section if the taxpayer uses a normalization method of accounting, or

"(C) the applicable 1968 method, if, with respect to its pre-1970 public utility property of the same (or similar) kind most recently placed in service, the taxpayer used a flow-through method of accounting for its July 1969 accounting period.

"(3) DEFINITIONS.—For purposes of this subsection—

"(A) PUBLIC UTILITY PROPERTY.—The term 'public utility property' means property used predominantly in the trade or business of the furnishing or sale of—

"(i) electrical energy, water, or sewage disposal services,

"(ii) gas or steam through a local distribution system,

"(iii) telephone services, or other communication services if furnished or sold by the Communications Satellite Corporation for purposes authorized by the Communications Satellite Act of 1962 (47 U.S.C. 701), or

"(iv) transportation of gas or steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof.

"(B) PRE-1970 PUBLIC UTILITY PROPERTY.—The term 'pre-1970 public utility property' means property which was public utility prop-

erty in the hands of any person at any time before January 1, 1970.

"(C) POST-1969 PUBLIC UTILITY PROPERTY.—The term 'post-1969 public utility property' means any public utility property which is not pre-1970 public utility property.

"(D) APPLICABLE 1968 METHOD.—The term 'applicable 1968 method' means, with respect to any public utility property—

"(i) the method of depreciation used on a return with respect to such property for the latest taxable year for which a return was filed before August 1, 1969,

"(ii) if clause (i) does not apply, the method used by the taxpayer on a return for the latest taxable year for which a return was filed before August 1, 1969, with respect to its public utility property of the same kind (or if there is no property of the same kind, property of the most similar kind) most recently placed in service, or

"(iii) if neither clause (i) nor (ii) applies, a subsection (l) method.

In the case of any section 1250 property to which subsection (j) applies, the term 'applicable 1968 method' means the method permitted under subsection (j) which is most nearly comparable to the applicable 1968 method determined under the preceding sentence.

"(E) APPLICABLE 1968 METHOD IN CERTAIN CASES.—If the taxpayer evidenced the intent to use a method of depreciation (other than its applicable 1968 method or a subsection (l) method) with respect to any public utility property in a timely application for change of accounting method filed before August 1, 1969, or in the computation of its tax expense for purposes of reflecting operating results in its regulated books of account for its July 1969 accounting period, such other method shall be deemed to be applicable 1968 method with respect to

such property and public utility property of the same (or similar) kind subsequently placed in service.

"(F) SUBSECTION (l) METHOD.—The term 'subsection (l) method' means any method determined by the Secretary or his delegate to result in a reasonable allowance under subsection (a), other than (i) a declining balance method, (ii) the sum of the years-digits method, or (iii) any other method allowable solely by reason of the application of subsection (b)(4) or (j)(1)(C).

"(G) NORMALIZATION METHOD OF ACCOUNTING.—In order to use a normalization method of accounting with respect to any public utility property—

"(i) the taxpayer must use the same method of depreciation to compute both its tax expense and its depreciation expense for purposes of establishing its cost of service for ratemaking purposes and for reflecting operating results in its regulated books of account, and

"(ii) if, to compute its allowance for depreciation under this section, it uses a method of depreciation other than the method it used for the purposes described in clause (i), the taxpayer must make adjustments to a reserve to reflect the deferral of taxes resulting from the use of such different methods of depreciation.

"(H) FLOW-THROUGH METHOD OF ACCOUNTING.—The taxpayer used a 'flow-through method of accounting' with respect to any public utility property if it used the same method of depreciation (other than a subsection (l) method) to compute its allowance for depreciation under this section and to compute its tax expense for purposes of reflecting operating results in its regulated books of account.

"(I) JULY 1969 ACCOUNTING PERIOD.—The term 'July 1969 accounting period' means the taxpayer's latest accounting period ending before August 1, 1969, for which it computed its

tax expense for purposes of reflecting operating results in its regulated books of account.

For purposes of this paragraph, different declining balance rates shall be treated as different methods of depreciation.

"(4) SPECIAL RULES AS TO FLOW-THROUGH METHOD.—

"(A) ELECTION AS TO NEW PROPERTY REPRESENTING GROWTH IN CAPACITY.—If the taxpayer makes an election under this subparagraph within 180 days after the date of the enactment of this subparagraph in the manner prescribed by the Secretary or his delegate, in the case of taxable years beginning after December 31, 1970, paragraph (2)(C) shall not apply with respect to any post-1969 public utility property, to the extent that such property constitutes property which increases the productive or operational capacity of the taxpayer with respect to the goods or services described in paragraph (3)(A) and does not represent the replacement of existing capacity.

"(B) CERTAIN PENDING APPLICATIONS FOR CHANGES IN METHOD.—In applying paragraph (1)(B), the taxpayer shall be deemed to have used a flow-through method of accounting for its July 1969 accounting period with respect to any pre-1970 public utility property for which it filed a timely application for change of accounting method before August 1, 1969, if with respect to public utility property of the same (or similar) kind most recently placed in service, it used a flow-through method of accounting for its July 1969 accounting period.

"(5) REORGANIZATIONS, ASSETS ACQUISITIONS, ETC.—If by reason of a corporate reorganization, by reason of any other acquisition of the assets of one taxpayer by another taxpayer, by reason of the fact that any trade or business of the taxpayer is subject to ratemaking by more than one body, or by reason of other circumstances, the application of any provisions

of this subsection to any public utility property does not carry out the purposes of this subsection, the Secretary or his delegate shall provide by regulations for the application of such provisions in a manner consistent with the purposes of this subsection."

(b) EFFECTIVE DATE.—The amendment made by subsection (a) shall apply with respect to all taxable years for which a return has not been filed before August 1, 1969.